HUSBAND AND WIFE, DIVORCE AND SEPARATION

This Help Sheet explains how husbands and wives are treated for Capital Gains Tax. The first part deals with transfers between spouses who are living together. The second part is concerned with the situation where separation has occurred. But it is only an introduction. If you are in any doubt about your circumstances you should ask your tax adviser. Your Inland Revenue office will also be pleased to help you, and provide those forms you may require. You can also consult the Inland Revenue Capital Gains Manual, which explains the rules in more detail. The Manual is available on the Inland Revenue website at www.inlandrevenue.gov.uk or you can ask to see it at your local Inland Revenue Enquiry Centre.

This Help Sheet will help you fill in the Capital Gains Pages of your Tax Return.

CAPITAL GAINS TAX LIABILITY

You and your spouse are treated as separate individuals for Capital Gains Tax purposes. Each of you will pay tax only on your own gains and you will get relief only for your own losses. However, although you are taxed separately, you may be treated as 'connected' with each other and with each other's relatives for certain purposes.

If you and your spouse are living together, any transfer of an asset between you is treated as giving rise to neither a gain nor a loss to the spouse transferring it. Any amount actually paid is ignored. If the spouse receiving the asset later disposes of it, he or she will be treated as if they had paid an amount equal to the total of your costs. The phrase 'living together' is defined on page 2.

If you are not living together, or the asset involved is trading stock, any asset transferred between you is treated as transferred at its market value at the time of the transfer. So, in these circumstances, the person transferring the asset may make a chargeable gain or an allowable loss. Similarly, any asset transfered at the time of death is treated as acquired at its market value at that date. But in that case there is no chargeable gain or allowable loss.

For transfers on death ask the Orderline for *Help Sheet IR282: Death, Personal Representatives and Legatees*. In general a person who inherits from their late spouse is treated the same as any other person who inherits on death.

Example 1

Mr Smith bought a non-business asset for £5,000 in March 1984. He sold the asset to his wife for £50,000 in September 1989 when they were living together.

The asset is deemed to have been transferred for an amount which gives neither a gain nor a loss on transfer. The actual amount paid by Mrs Smith is ignored.

The deemed disposal proceeds are calculated as follows:

Cost	£5,000
plus indexation allowance March 1984 to September 1989 £5,000 x 0.333	£1,665
Deemed disposal proceeds	£6,665

Mr Smith has neither a gain nor a loss.

The deemed cost to Mrs Smith for any future disposal of the asset is £6,665.

Mrs Smith sells the asset for £20,000 in June 2000. The gain arising is:

Disposal proceeds	£20,000
minus cost	£6,665
Unindexed gain	£13,335
minus indexation allowance September 1989 to April 1998 based on cost of £6,665 x 0.395	£2,633
Net chargeable gain	£10,702

Note: Indexation allowance has been frozen in the computation of chargeable gains accruing on or after 6 April 1998. So indexation allowance is computed only to April 1998.

ASSETS HELD IN YOUR NAME

You are chargeable to Capital Gains Tax if you dispose of an asset held in your name, unless you are holding it on behalf of another person, such as your spouse. If you are holding an asset on behalf of your spouse, your spouse is commonly known as the beneficial owner and will pay tax if a gain is made from its disposal. To decide which of you should return any gain and pay any tax, you should consider:

- whether you and your spouse have made a formal declaration about beneficial ownership using form 17
- who provided the cost price and whether the asset was bought as a gift for your spouse
- who received the proceeds of the disposal.

INDEXATION ALLOWANCE

In calculating any chargeable gain, you can deduct an additional allowance, called the indexation allowance, which is explained in the Notes on Capital Gains.

In the computation of chargeable gains accruing on or after 6 April 1998 indexation allowance has been frozen. This means that indexation allowance will be given for periods up to April 1998, but not after then.

Special rules apply where an asset that has been transferred between a husband and wife is finally disposed of. If the last transfer between husband and wife occurred before 30 November 1993 the deemed cost, including the indexation allowance, is allowable in full against any proceeds received when the asset is disposed of. If the last transfer between husband and wife occurred on or after 30 November 1993, the amount of indexation allowance included in the deemed cost may be restricted when the asset is finally disposed of. It is not available to create or increase any loss.

Example 2

Mr Jones bought an asset for £10,000 in March 1985. He transferred the asset to his wife in December 1993. The deemed cost to Mrs Jones for any future disposal of the asset is:

Cost	£10,000
plus indexation allowance March 1985 to December 1993 £10,000 x 0.529	£5,290
Deemed cost	£15,290

Mrs Jones sells the asset for £12,000 in April 2000. The loss arising is:

Disposal proceeds	£12,000
minus cost	£15,290
Unindexed loss	(£3,290)
plus Indexation	0
Allowable loss	(£3,290)

However, the cost includes indexation allowance of £5,290. As this is greater than the amount of the allowable loss calculated, it is restricted to the amount required to reduce the allowable loss to zero. The figure allowed is therefore £2,000 (£5,290 *minus* £3,290). Mrs Jones is treated as making neither a gain nor a loss.

No indexation allowance is due on the sale as this would increase the loss.

One important point to note is that if the husband or wife transferring the asset to the other spouse held the asset on 31 March 1982 and the final disposal took place on or after 6 April 1988, the asset is deemed, for rebasing purposes, to have been held at 31 March 1982 by the spouse who made that disposal.

TAPER RELIEF

Taper relief was introduced in the Finance Act 1998 to replace indexation allowance for periods after 5 April 1998. For further information ask the Orderline for *Help Sheet IR279: Taper relief*.

Where an asset which has been transfered from one spouse to the other is later sold, the qualifying holding period for taper relief purposes is the combined period of ownership of both spouses after 5 April 1998. A bonus year may be added where the asset was acquired by either spouse before 17 March 1998 and still held at 6 April 1998. So in Example 1 the disposal in June 2000 is tapered at the three year rate.

WHAT COUNTS AS 'LIVING TOGETHER'

You and your spouse are treated as living together unless:

- you are separated under a court order, **or**
- you are separated by a formal Deed of Separation executed under seal (in Scotland a deed should be witnessed), **or**
- you are separated in such circumstances that the separation is likely to be permanent.

In each case the marriage must have broken down. If the marriage has not broken down but the two of you do not live in the same house you are still treated as living together for Capital Gains Tax purposes.

SEPARATION AND DIVORCE

The remainder of this Help Sheet explains your Capital Gains Tax liability if you are separated or divorced and you have transferred assets to the spouse from whom you are separated, or to a former spouse from whom you are divorced.

YEAR OF PERMANENT SEPARATION

If you or your spouse were living together at some time in a tax year, you can transfer assets between you at any time in that tax year at no gain/no loss. There is no requirement that you should be living together at the time of transfer.

Example 3

Mr Brown transferred an asset to Mrs Brown on 30 June 2000. Mr and Mrs Brown separated on 1 December 2000. Mr Brown transferred another asset to Mrs Brown on 1 March 2001.

Both transfers take place for an amount which gives neither a gain nor a loss to Mr Brown. Transfers may take place on this basis until and including 5 April 2001 even though the couple were not living together from 1 December 2000.

If a transfer occurs between you and your spouse after the end of the tax year in which you stop living together, there are rules to decide the date of disposal and the amount of consideration on disposal. These rules depend on your particular circumstances and the information you will need is as follows:

- the date of any decree absolute
- the date of the court order if the asset was transferred by such an order
- the date of any other contract under which the asset was transferred.

As the rules are complicated, they are not included in this Help Sheet. Once you hold the necessary information, ask your Inland Revenue office or tax adviser for advice.

PRIVATE RESIDENCE RELIEF

You and your spouse, while living together, can only have one only or main residence between you, and private residence relief may only be due on any gain arising on disposal of that residence. Following separation, each of you may have a different only or main residence and each may be entitled to relief on any gains arising on the disposal of the residence(s).

Where, as part of a financial settlement on separation or divorce, the spouse who has ceased to occupy the matrimonial home transfers an interest in that home to the other spouse, and the date of transfer takes place more than three years after the time when the spouse last occupied the matrimonial home, full private residence relief will not be due. However, the former matrimonial home can be treated as the only or main residence of the transferring spouse from the date his or her occupation ceased until the earlier of:

- the date of transfer
- the date on which the spouse to whom the property is transferred ceases to use it as his or her only or main residence.

However, relief for the same period cannot be given for another property (except for the final three years of ownership of the matrimonial home) so this concession may not be the best choice in every case.

RETIREMENT RELIEF

If you have acquired the whole of your spouse's business interest you may be able to elect to have retirement relief by reference to the joint period in business. But you and your spouse must have been living together in the tax year in which the business interest was transferred to qualify. To find out more ask the Orderline for *Help Sheet IR289: Retirement relief and Capital Gains Tax.*

HOLD-OVER RELIEF

If an asset is transferred from one spouse to the other after the end of the tax year in which separation took place, the transfer is treated as taking place at market value. The conditions for a claim to hold-over relief may be satisfied. However, in these circumstances, it is important to know whether any consideration was given by the spouse receiving the asset.

Usually the asset is transferred in exchange for a surrender, by the recipient, of rights they would otherwise be able to exercise to obtain alternative financial provision. In such cases the value of the rights surrendered is actual consideration of an amount that would eliminate any hold-over relief. To find out more ask the Orderline for *Help Sheet IR295: Relief for gifts and similar transactions.*

These notes are for guidance only, and reflect the position at the time of writing. They do not affect any rights of appeal.